

# *Research on Financial Cooperation between China and Pakistan*

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**Abstract:** Pakistan is an important economic partner of China, with strong economic complementarity and broad prospects for financial cooperation. Therefore, there is enormous potential for cooperation between the two sides in the financial field. However, there are currently some problems in the financial cooperation between the two countries, which have a hindering impact on the subsequent development of their cooperation. In view of this, this article will study some of the problems that exist in the financial cooperation between the two parties and propose some suggestions, hoping to provide reference and assistance.

## 1. Introduction

Since the "the Belt and Road" initiative was put forward, the cooperation between China and Pakistan has developed rapidly. At present, Pakistan has become an important economic partner of China in South Asia, and the two sides have certain complementarity in industrial structure, energy, trade, infrastructure construction, and other aspects. In recent years, with the implementation of the "the Belt and Road" initiative, China Pakistan relations have made great progress and cooperation fields have been expanding. Especially in the financial field, both sides have made significant progress in currency swaps, bond issuance, and securities trading. Therefore, in order to promote further cooperation, it is necessary to analyze and study the financial cooperation issues between the two sides.

## 2. Problems in China Pakistan financial cooperation

### 2.1. Foreign exchange risk

At present, Pakistan's foreign exchange rate fluctuates greatly, often experiencing sudden increases or decreases in foreign exchange rates. In this situation, enterprises will face higher risks, which requires them to increase their attention to the foreign exchange market and use financial means to avoid risks<sup>[1]</sup>. At the same time, foreign exchange trading and investment can also be conducted through various methods, as shown in Table 1.

Based on Table 1, although there is some room for choice in the foreign exchange trading and investment methods of both parties, in reality, Chinese companies are subject to many restrictions in

their choice of financial instruments when investing in Pakistan, leading to an increase in foreign exchange risks. Pakistan has implemented strict foreign exchange control policies, and the approval time for overseas payments is at least one month, which has led to an extended collection cycle and increased collection costs for Chinese enterprises, affecting the efficiency of their capital utilization. At the same time, enterprises will also face risks of foreign exchange policy instability and anti money laundering review.

Table 1: Main Methods of Foreign Exchange Trading and Investment

Main way	Commercial bank
	Bond
	Share certificate

## 2.2. Market Risk

Market risk refers to the risk of investment returns and costs deviating due to market price fluctuations, and Pakistan's financial market amplifies such risks. Table 2 shows the characteristics of Pakistan's financial market.

Table 2: Characteristics and Reasons of Pakistan's Financial Market

Characteristic	Reason
Poor stability of the financial system	Pakistan's financial system is not well-developed and lacks corresponding laws and regulations to maintain its stability
The domestic economic development level is relatively low	Pakistan's domestic government policies are constantly changing, which has led to unstable economic policies and a lack of long-term planning, resulting in a lower level of economic development
Inflation and low interest rates	Due to the low level of economic development, there has been inflation and low interest rates in Pakistan

The above issues will have a significant impact on the economic benefits of Chinese enterprises, especially after the financial crisis, when exchange rate fluctuations are even greater, which will have a serious impact on enterprises. Meanwhile, in recent years, prices in Pakistan have continued to rise, with severe inflation far exceeding that of China and the global average. The high inflation rate has raised the cost of financial cooperation between China and Pakistan, increasing the possibility of financial risks.

## 2.3. Market Differences

For one thing, the bilateral trade structure between China and Pakistan is unreasonable. At present, China's exports to Pakistan mainly consist of electromechanical products and agricultural products, while Pakistan's exports to China are mainly primary products with a low proportion of industrial manufactured goods. Most of Pakistan's industrial manufactured goods need to be imported, which has had a significant impact on its domestic market. At the same time, due to the small domestic market in Pakistan, its export products have relatively low prices, which makes it lack competitiveness in the international market<sup>[2]</sup>. Therefore, the unreasonable trade structure between China and Pakistan will constrain their cooperation in the financial field.

For another, the level of economic development in Pakistan is relatively low. The imperfect domestic banking system, lagging financial market development, and strict foreign exchange controls in Pakistan pose certain risks to its direct investment in China<sup>[3]</sup>. This also leads to a lack of sufficient financial support and safeguard measures for Pakistan's investment in China, which will bring huge

risks to China Pakistan cooperation in the financial field.

## **2.4. The development of Pakistan's financial market lags behind**

The development of Pakistan's financial market lags behind, and the concentration of the banking industry is high, making it difficult to meet the long-term financing needs of Chinese enterprises. This centralized pattern makes the funding sources of Pakistani banks very single, and their credit business mainly focuses on short-term loans, which is difficult to meet the long-term financing needs of Chinese enterprises. Additionally, there are certain issues with the banking structure in Pakistan. At present, there is an imbalance in the proportion of commercial banks, rural financial institutions, and public sector financial institutions in Pakistan, leading to fierce market competition<sup>[4-5]</sup>. At the same time, due to the service deficiencies of domestic banks in Pakistan, their loan interest rates are relatively high, while the loan costs for Chinese enterprises are relatively low. The financing for China Pakistan financial cooperation mainly comes from Chinese financial institutions, which makes the financing source relatively single. With the expansion of China Pakistan trade scale, a large amount of financial support is needed in the future, and a single financing channel will not be able to meet investment needs. China Pakistan financial cooperation needs to broaden financing channels and address financing constraints through multiple channels such as international financial cooperation, utilization of international capital, and currency exchange.

## **2.5. Policy and social environmental risks**

The China Pakistan Economic Corridor is an important economic, trade, and energy corridor for China in West Asia, South Asia, Europe, and Africa, playing a crucial role in safeguarding China's national security and economic development. The financial cooperation between China and Pakistan is mainly driven by Chinese investment, but due to the fact that the cooperation projects of the China Pakistan Economic Corridor are mainly located in Pakistan, the financial cooperation between China and Pakistan is highly dependent on the coordination of the Pakistani government. However, due to the instability and inconsistency of Pakistani policies, China Pakistan investment faces huge financial risks. Meanwhile, the construction of the China Pakistan Economic Corridor has aroused hostility from the United States, India, and anti China forces within Pakistan, as they unilaterally believe that China Pakistan cooperation will affect their interests in the Middle East, South Asia, and Central Asian countries. At the same time, there are many unstable factors in Pakistan's political situation, including differences in interests among various political parties and religions in the country regarding the China Pakistan cooperation project, difficulty in unifying opinions between the government and military, and numerous military coups. Finally, the domestic legal system in Pakistan is not yet sound, and there is a certain degree of arbitrariness in law enforcement, such as the problem of frequent changes in cooperation projects, which has led to a certain number of litigation cases.

## **3. Solutions and Development Suggestions for Financial Cooperation between China and Pakistan**

### **3.1. Solutions to Problems**

The financial cooperation between China and Pakistan is a long-term process, and with the joint efforts of both sides, the financial cooperation between the two countries will become increasingly close. But there are also some problems that hinder the further development of financial cooperation between the two sides<sup>[6]</sup>. To address these issues, this article proposes the following suggestions.

Firstly, strengthen cooperation between both parties in currency exchange. In currency exchange

between both parties, there should be clear regulations on the scale and duration of currency exchange, so that banks can better use this financial instrument. As one of the countries along the "the Belt and Road", Pakistan's currency is also one of the important currencies in trade with China. The two countries should strengthen currency exchange and cooperation to facilitate trade between Pakistan and China<sup>[7]</sup>. Meanwhile, the two countries can continue to explore more forms and channels of currency exchange.

Secondly, increase support for related industries in Pakistan. Pakistan is an agricultural country, and its domestic agriculture is relatively backward, so China needs to increase its investment in agriculture. Both sides should encourage and support agricultural enterprises to invest, develop, and produce in Pakistan, and provide them with certain tax incentives. At the same time, we can actively guide agricultural enterprises to invest in Pakistan and encourage them to develop deep processing industries locally, in order to export agricultural products to other countries.

Thirdly, accelerate the training of financial talents in both countries. At present, China has cultivated a group of high-quality talents in the financial field, but there is still a shortage in the number of financial talents. Therefore, we should vigorously develop higher education and vocational education, and encourage talents to exchange, study and work in Pakistan. At the same time, it can also strengthen cooperation and educational cooperation in the field of financial talent between the two sides, in order to enhance the overall level of China's financial sector in Pakistan and the quality of relevant personnel<sup>[8]</sup>.

Fourthly, promote the development of cooperation projects between the two countries in the financial sector. The two countries can jointly promote the development of financial cooperation projects between China and Pakistan with strong support from their respective governments. For example, the banks of the two countries can be united to form a regional bank and provide some preferential policies for the regional bank to better develop. A bilateral bank can also be established to utilize the resources of both sides and to improve the level of cooperation in the financial field to a certain extent.

Finally, pay attention to the political situation in Pakistan, timely obtain information on the domestic political situation in Pakistan, and establish a mechanism for information disclosure and transmission. At the same time, utilizing the influence of Pakistani private think tanks and media to positively promote the positive significance of the China Pakistan Economic Corridor and China Pakistan financial cooperation for both countries, establish a positive image of China, and urge various political parties and forces in Pakistan to reach a consensus on China Pakistan economic cooperation. In addition, by improving relevant laws and regulations on international financial cooperation, it can provide legal protection for Chinese enterprises and financial institutions to engage in foreign financial cooperation, establish insurance mechanisms related to international business cooperation, and provide corresponding guarantees for international investments of various financial institutions

## **3.2. Future Development Suggestions**

### **3.2.1. Strengthen cooperation between the two countries in the securities market field**

First of all, strengthen cooperation between Chinese enterprises for direct financing in Pakistan. As China currently does not have the conditions to establish a stock exchange in Pakistan, both sides can first establish stock exchanges in both countries, so that Chinese and Pakistani enterprises can trade on the stock exchanges of both countries. If both securities markets can be established, trading between the two countries' securities markets will be more convenient and efficient. In addition, if a cooperation mechanism can be established between the securities markets of the two countries, it will also contribute to the cooperation between the securities markets of the two countries<sup>[9]</sup>.

Next, encourage Chinese enterprises to invest and develop in Pakistan. Chinese enterprises investing and developing in Pakistan can help alleviate the pressure on Chinese enterprises to "go global" and promote the development of the Chinese economy. At the same time, Chinese enterprises should be encouraged to make long-term investments and development in Pakistan in order to enhance the cooperation between the two countries' economies. In addition, Chinese financial institutions investing in Pakistan is conducive to expanding China's influence in Pakistan and promoting cooperation between the Chinese and Pakistani economies. At the same time, it can also increase the depth and breadth of financial cooperation between China and Pakistan.

Finally, accelerate the establishment of a mechanism for interconnectivity between the capital markets of the two countries. The development of the securities market between the two countries has unique conditions and foundations, so it is necessary to accelerate the establishment of a capital market interconnection mechanism between the two countries, in order to facilitate further cooperation and win-win outcomes between the economies of China and Pakistan.

### **3.2.2. Strengthen cooperation between the two countries in the insurance market**

Pakistan is a developing country, and its domestic insurance industry is still in its early stages of development, but the insurance market in Pakistan is relatively small. China can establish some insurance institutions in Pakistan to provide more insurance products for Pakistan, and also provide more insurance protection for China's exports to Pakistan. In addition, China can also provide more financial and technological support and assistance to Pakistan to facilitate its better development.

For one thing, promote the China Pakistan insurance talents training project. At present, China has established some insurance institutions which have provided great assistance for the development of Chinese enterprises overseas. However, these financial institutions are all profit oriented, so their requirements for talent are relatively high. China needs a group of financial talents with strong professional knowledge and professional qualities to manage overseas. Pakistan is relatively weak in this regard, therefore, China should strengthen cooperation with Pakistan in talent cultivation<sup>[10]</sup>.

For another, improve the cooperation between the two countries in the capital market. At present, there are not many cooperation projects between China and Pakistan in the capital market. Due to the fact that the capital market is an industry with relatively slow information transmission, the two countries should further improve information communication and exchange channels in the capital market.

### **3.2.3. Strengthen cooperation between the two countries in the commercial banking field**

Firstly, strengthen cooperation between China and Pakistan in credit cooperation for small and medium-sized enterprises. The two governments should strengthen cooperation and support in credit for small and medium-sized enterprises, in order to enable more small and medium-sized enterprises to obtain bank loans and alleviate the funding shortage they encounter in their development. At the same time, small and medium-sized enterprise loan projects can also be used to encourage enterprises from both countries to invest and trade in each other's countries, promoting common economic development between the two countries.

Then, invite the Pakistani government to visit our country for inspection and exchange. Although the two countries have not yet established a bilateral currency exchange mechanism, a development model of "new leading old" has been formed in the construction of the China Pakistan Economic Corridor. So the two governments can strengthen the construction of bilateral currency swap mechanisms, while also promoting the deepening of the construction of the China Pakistan Economic Corridor.

Finally, support win-win cooperation between enterprises from both countries. At present, the

economic ties between China and Pakistan are becoming increasingly close, and the cooperation between the two countries in trade and investment is also increasing. Therefore, both countries should encourage cooperation and win-win outcomes among enterprises in order to promote the smooth construction of the China Pakistan Economic Corridor.

#### 4. Conclusion

In summary, in order to promote financial cooperation between China and Pakistan, both sides should solve the problem of insufficient funds by strengthening talent training and infrastructure construction in relevant fields, and continuously expand the scope and scale of the use of the RMB in Pakistan to promote bilateral trade and investment, further promote the facilitation of trade and investment between the two countries to promote the development of trade and investment, promote the establishment of a bilateral currency exchange agreement between China and Pakistan, and deepen the degree of financial cooperation between the two sides.

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